

Federal Reserve System

§ 226.35

other third-party documents that provide reasonably reliable evidence of the consumer's income or assets.

(B) Notwithstanding paragraph (a)(4)(ii)(A), a creditor has not violated paragraph (a)(4)(ii) if the amounts of income and assets that the creditor relied upon in determining repayment ability are not materially greater than the amounts of the consumer's income or assets that the creditor could have verified pursuant to paragraph (a)(4)(ii)(A) at the time the loan was consummated.

(C) A creditor must verify the consumer's current obligations.

(iii) *Presumption of compliance.* A creditor is presumed to have complied with this paragraph (a)(4) with respect to a transaction if the creditor:

(A) Verifies the consumer's repayment ability as provided in paragraph (a)(4)(ii);

(B) Determines the consumer's repayment ability using the largest payment of principal and interest scheduled in the first seven years following consummation and taking into account current obligations and mortgage-related obligations as defined in paragraph (a)(4)(i); and

(C) Assesses the consumer's repayment ability taking into account at least one of the following: The ratio of total debt obligations to income, or the income the consumer will have after paying debt obligations.

(iv) *Exclusions from presumption of compliance.* Notwithstanding the previous paragraph, no presumption of compliance is available for a transaction for which:

(A) The regular periodic payments for the first seven years would cause the principal balance to increase; or

(B) The term of the loan is less than seven years and the regular periodic payments when aggregated do not fully amortize the outstanding principal balance.

(v) *Exemption.* This paragraph (a)(4) does not apply to temporary or "bridge" loans with terms of twelve months or less, such as a loan to purchase a new dwelling where the consumer plans to sell a current dwelling within twelve months.

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§ 226.35 Prohibited acts or practices in connection with higher-priced mortgage loans.

(a) *Higher-priced mortgage loans*—(1) For purposes of this section, a higher-priced mortgage loan is a consumer credit transaction secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 or more percentage points for loans secured by a

first lien on a dwelling, or by 3.5 or more percentage points for loans secured by a subordinate lien on a dwelling.

(2) "Average prime offer rate" means an annual percentage rate that is derived from average interest rates, points, and other loan pricing terms currently offered to consumers by a representative sample of creditors for mortgage transactions that have low-risk pricing characteristics. The Board publishes average prime offer rates for a broad range of types of transactions in a table updated at least weekly as well as the methodology the Board uses to derive these rates.

(3) Notwithstanding paragraph (a)(1) of this section, the term "higher-priced mortgage loan" does not include a transaction to finance the initial construction of a dwelling, a temporary or "bridge" loan with a term of twelve months or less, such as a loan to purchase a new dwelling where the consumer plans to sell a current dwelling within twelve months, a reverse-mortgage transaction subject to § 226.33, or a home equity line of credit subject to § 226.5b.

(b) *Rules for higher-priced mortgage loans.* Higher-priced mortgage loans are subject to the following restrictions:

(1) *Repayment ability.* A creditor shall not extend credit based on the value of the consumer's collateral without regard to the consumer's repayment ability as of consummation as provided in § 226.34(a)(4).

(2) *Prepayment penalties.* A loan may not include a penalty described by § 226.32(d)(6) unless:

(i) The penalty is otherwise permitted by law, including § 226.32(d)(7) if the loan is a mortgage transaction described in § 226.32(a); and

(ii) Under the terms of the loan—

(A) The penalty will not apply after the two-year period following consummation;

(B) The penalty will not apply if the source of the prepayment funds is a refinancing by the creditor or an affiliate of the creditor; and

(C) The amount of the periodic payment of principal or interest or both may not change during the four-year period following consummation.

(3) *Escrows*—(i) *Failure to escrow for property taxes and insurance.* Except as provided in paragraph (b)(3)(ii) of this section, a creditor may not extend a loan secured by a first lien on a principal dwelling unless an escrow account is established before consummation for payment of property taxes and premiums for mortgage-related insurance required by the creditor, such as insurance against loss of or damage to property, or against liability arising out of the ownership or use of the property, or insurance protecting the creditor against the consumer's default or other credit loss.

(ii) *Exemptions for loans secured by shares in a cooperative and for certain condominium units*—(A) Escrow accounts need not be established for loans secured by shares in a cooperative; and

(B) Insurance premiums described in paragraph (b)(3)(i) of this section need not be included in escrow accounts for loans secured by condominium units, where the condominium association has an obligation to the condominium unit owners to maintain a master policy insuring condominium units.

(iii) *Cancellation.* A creditor or servicer may permit a consumer to cancel the escrow account required in paragraph (b)(3)(i) of this section only in response to a consumer's dated written request to cancel the escrow account that is received no earlier than 365 days after consummation.

(iv) *Definition of escrow account.* For purposes of this section, “escrow account” shall have the same meaning as in 24 CFR 3500.17(b) as amended.

(4) *Evasion, open-end credit.* In connection with credit secured by a consumer's principal dwelling that does not meet the definition of open-end credit in § 226.2(a)(20), a creditor shall not structure a home-secured loan as an open-end plan to evade the requirements of this section.

[Reg. Z, 73 FR 44603, July 30, 2008]

EFFECTIVE DATE NOTE: By Reg. Z, 73 FR 44603, July 30, 2008, § 226.35 was added, effective October 1, 2009, except for (b)(3) which is effective on April 1, 2010.

§ 226.36 Prohibited acts or practices in connection with credit secured by a consumer's principal dwelling.

(a) *Mortgage broker defined.* For purposes of this section, the term “mortgage broker” means a person, other than an employee of a creditor, who for compensation or other monetary gain, or in expectation of compensation or other monetary gain, arranges, negotiates, or otherwise obtains an extension of consumer credit for another person. The term includes a person meeting this definition, even if the consumer credit obligation is initially payable to such person, unless the person provides the funds for the transaction at consummation out of the person's own resources, out of deposits held by the person, or by drawing on a bona fide warehouse line of credit.

(b) *Misrepresentation of value of consumer's dwelling*—(1) *Coercion of appraiser.* In connection with a consumer credit transaction secured by a consumer's principal dwelling, no creditor or mortgage broker, and no affiliate of a creditor or mortgage broker shall directly or indirectly coerce, influence, or otherwise encourage an appraiser to misstate or misrepresent the value of such dwelling.

(i) Examples of actions that violate this paragraph (b)(1) include:

(A) Implying to an appraiser that current or future retention of the appraiser depends on the amount at which the appraiser values a consumer's principal dwelling;

(B) Excluding an appraiser from consideration for future engagement because the appraiser reports a value of a consumer's principal dwelling that does not meet or exceed a minimum threshold;

(C) Telling an appraiser a minimum reported value of a consumer's principal dwelling that is needed to approve the loan;

(D) Failing to compensate an appraiser because the appraiser does not value a consumer's principal dwelling at or above a certain amount; and

(E) Conditioning an appraiser's compensation on loan consummation.

(ii) Examples of actions that do not violate this paragraph (b)(1) include: